

A Look at the Economy as we Approach 2011

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Summary

- The economic outlook has weakened since the spring
 - Downward revisions to historical data means we are starting from a lower point
 - The economic recovery entered a “soft patch” in the second quarter and the national outlook is now considerably weaker
- Economic activity is “muddling along” and the recovery is expected to be painfully slow
 - Weak confidence
 - Weak housing, commercial construction
 - Slow job growth
 - Improving, but still tight credit for small business
- Double-dip unlikely, but possibility higher



The worst recession since WW II ended in June 2009

Recession	Peak-to-trough decline		Recession Duration
	Real GDP	Employment	
	<i>percent</i>	<i>percent</i>	<i>months</i>
1948-49	1.6	5.0	11
1953-54	2.5	3.4	10
1957-58	3.1	4.2	8
1960-61	0.5	2.3	10
1969-70	0.2	1.2	11
1973-75	3.2	1.9	16
1980	2.2	2.3	6
1981-82	2.6	3.1	16
1990-91	1.4	1.4	8
2001	0.7	1.7	8
Average	1.8	2.6	10
2007-09	4.1	6.1	18

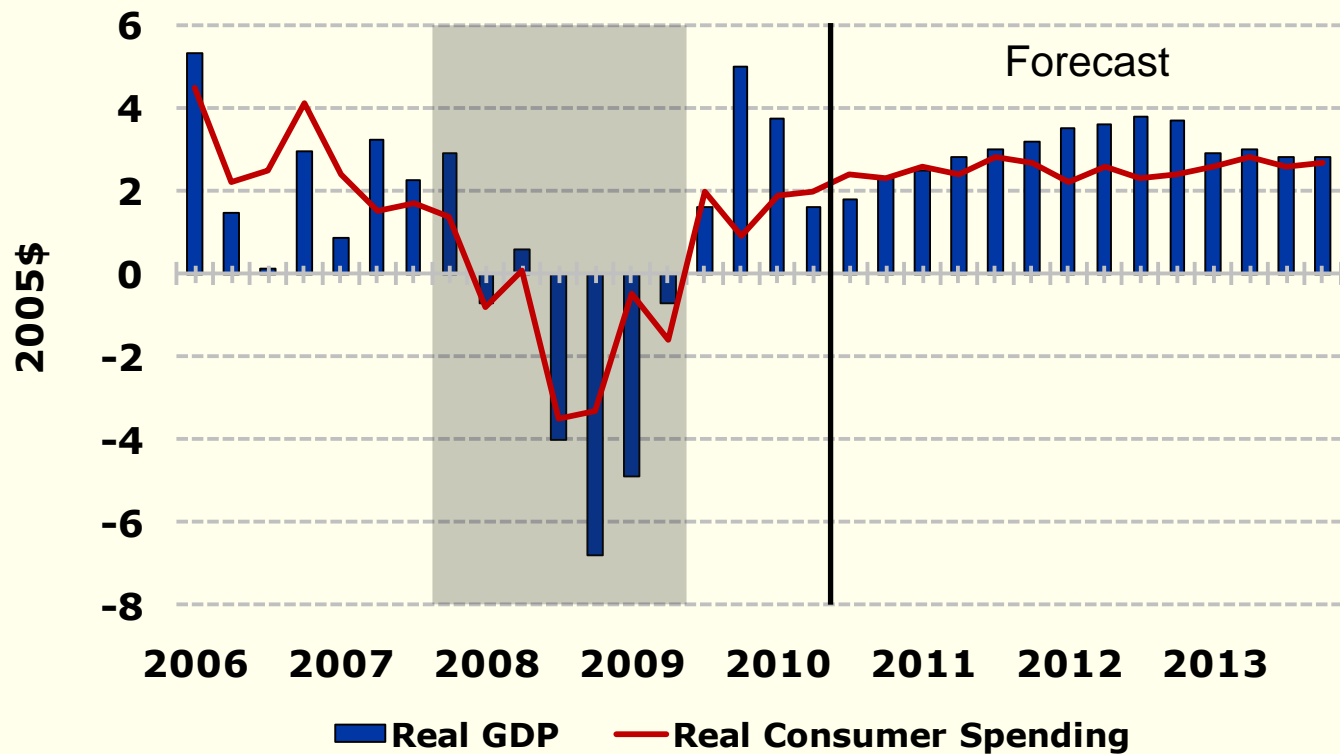
Source: NBER, ERFC

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GDP growth took off in 2009Q4 and 2010Q1 but then slowed

Percent growth, SAAR



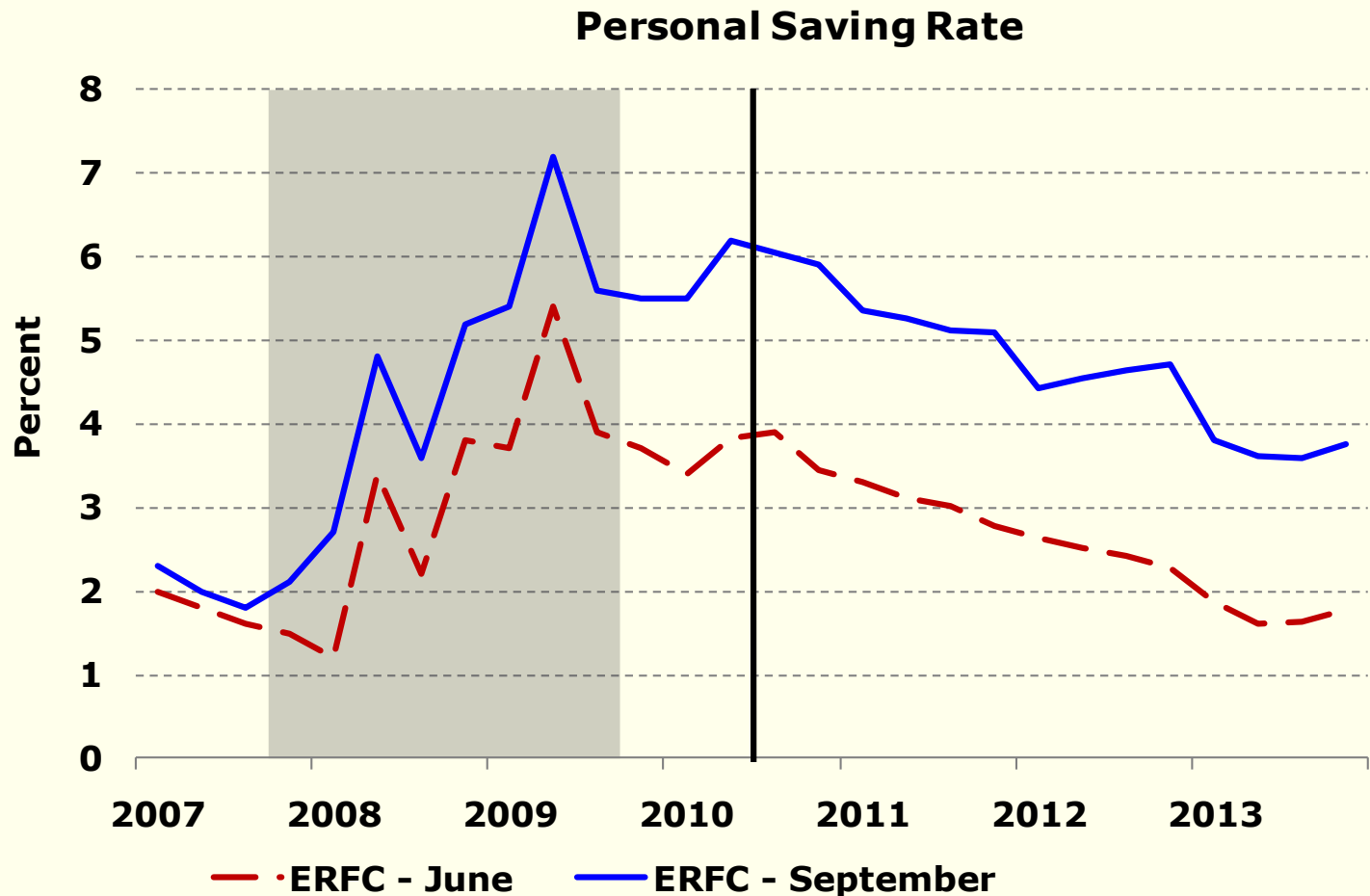
Source: BEA, data through 2010 Q2, ERFC forecast through 2013Q4

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The historical savings rate was revised up sharply in August

The saving rate for 2010Q1 was revised from 3.1% of disposable income to 5.5%.

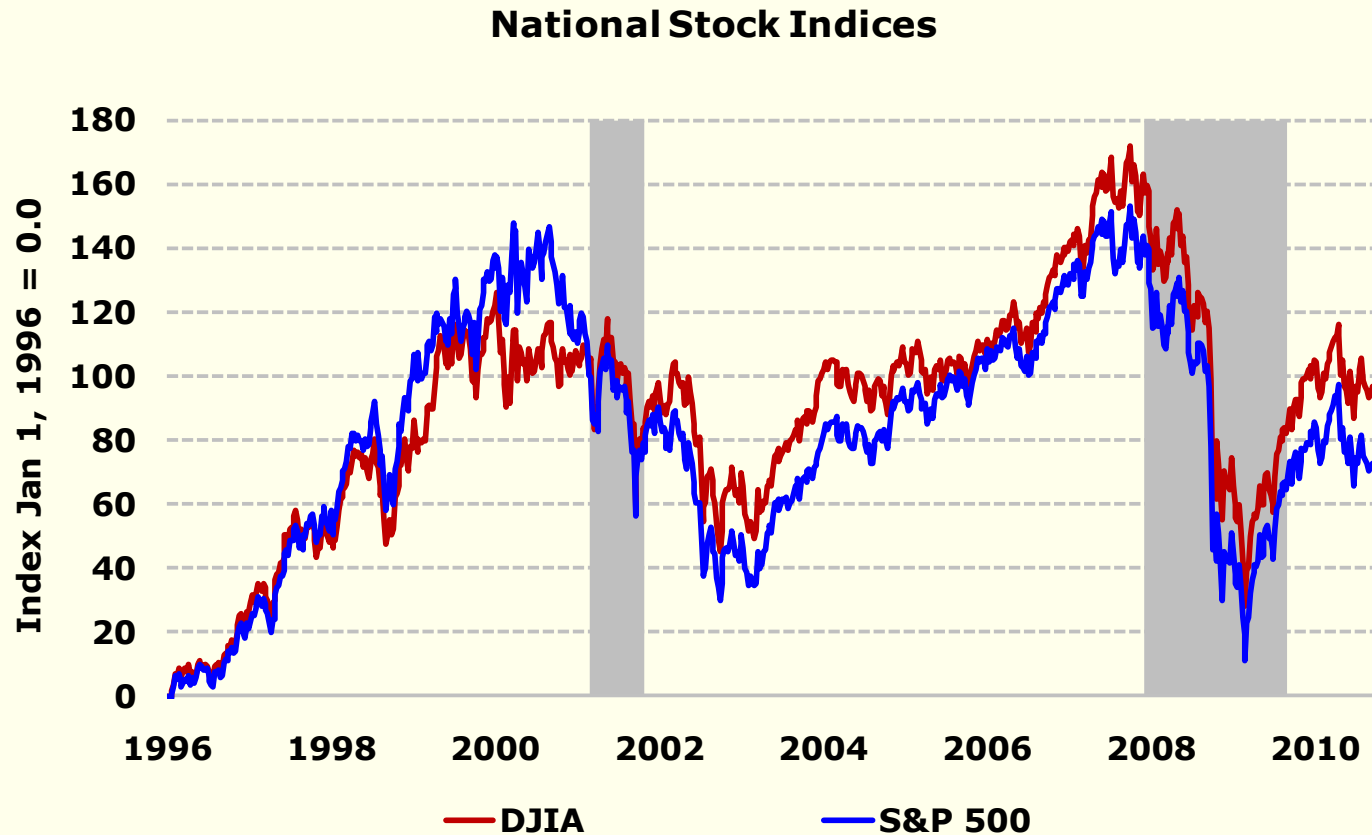


Source: ERFC September 2010 forecast; actual through 2010 Q2

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Equity markets are indicating a slowing of growth...



Source: Yahoo! Finance; data through September 24, 2010



... as are bond markets



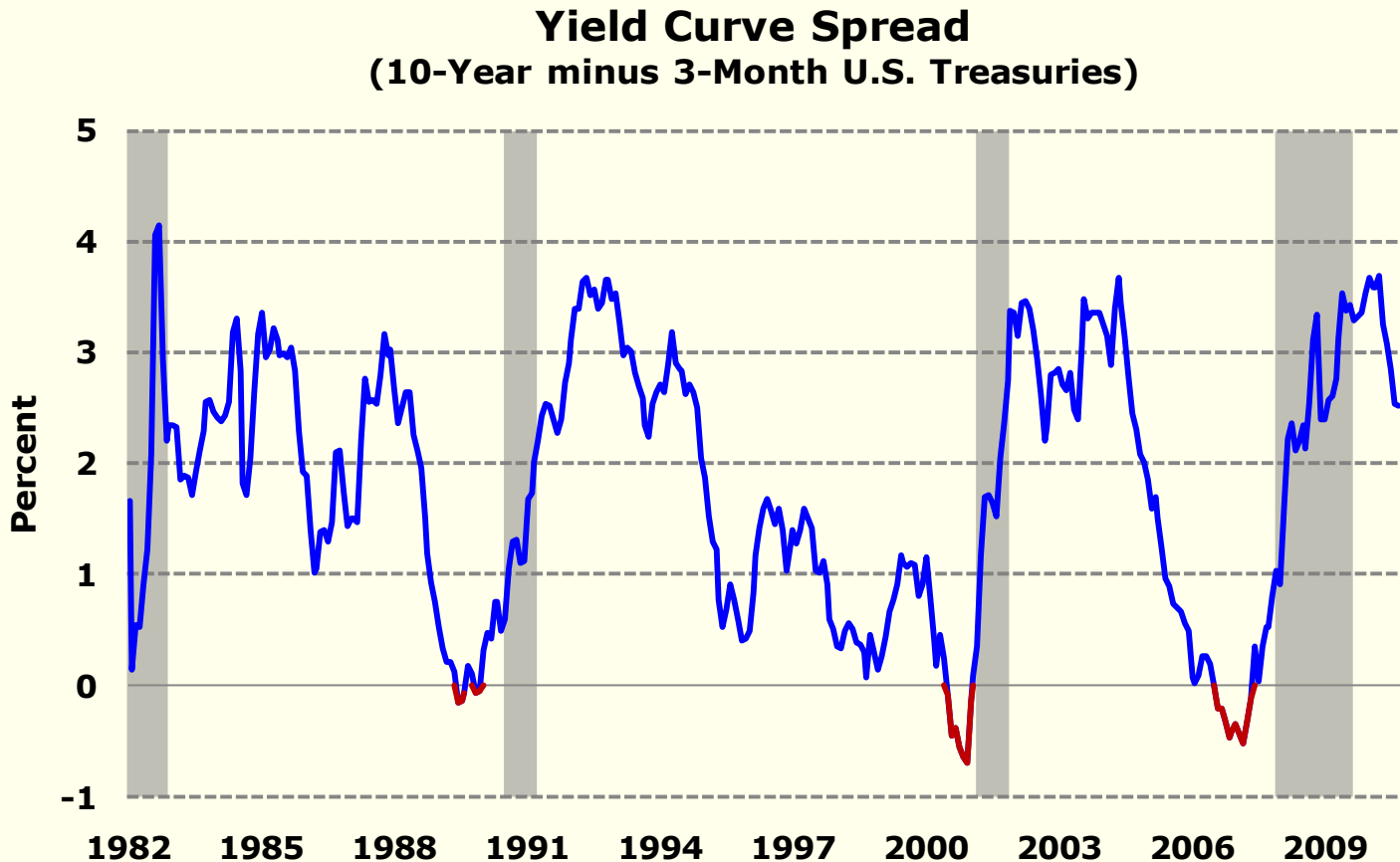
Source: Federal Reserve; data through September 28, 2010

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The yield curve has flattened, but is not signaling a double dip

An inverted yield curve typically precedes a recession while a steepening yield curve signifies a recovery



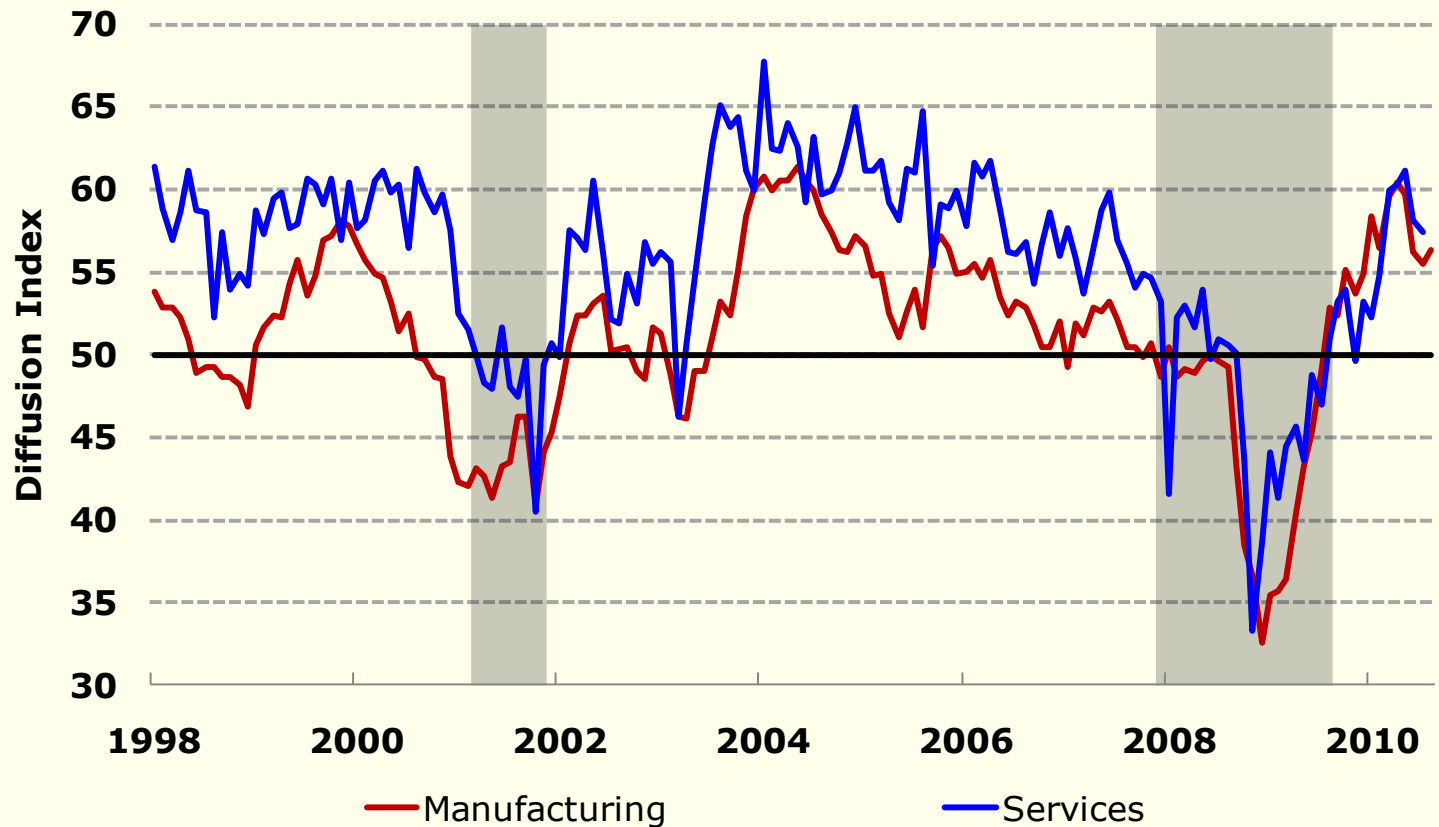
Source: Federal Reserve Board, ERFC; data through September 2010

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ISM indices for both services and manufacturing indicate moderating growth

An index greater than 50, implies growth



Source: Institute of Supply Management; data through August 2010

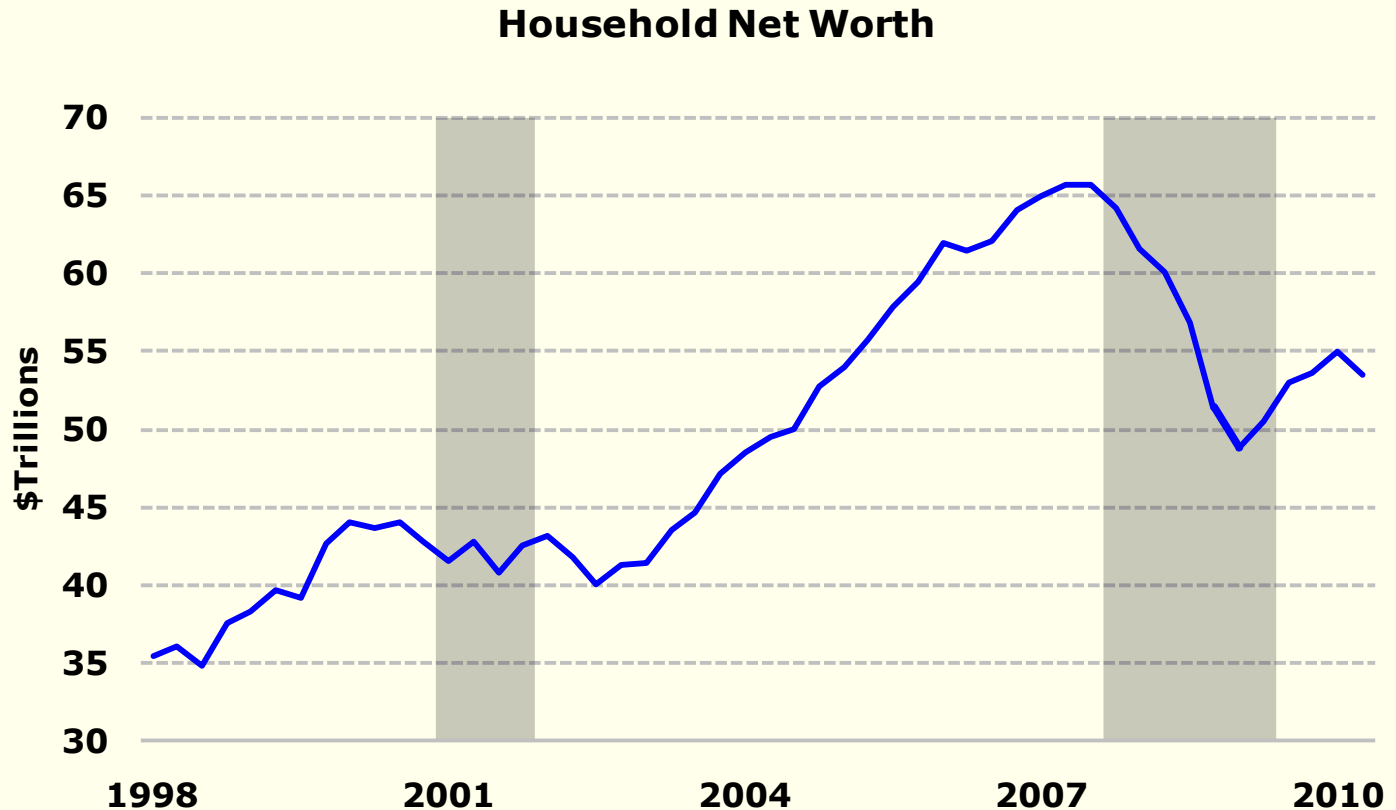
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Recovery in household net worth stalled in 2010Q2

\$18 trillion
of wealth
was lost in
this
recession

\$6 trillion
has been
recovered
so far



Source: Federal Reserve; data through 2010 Q2

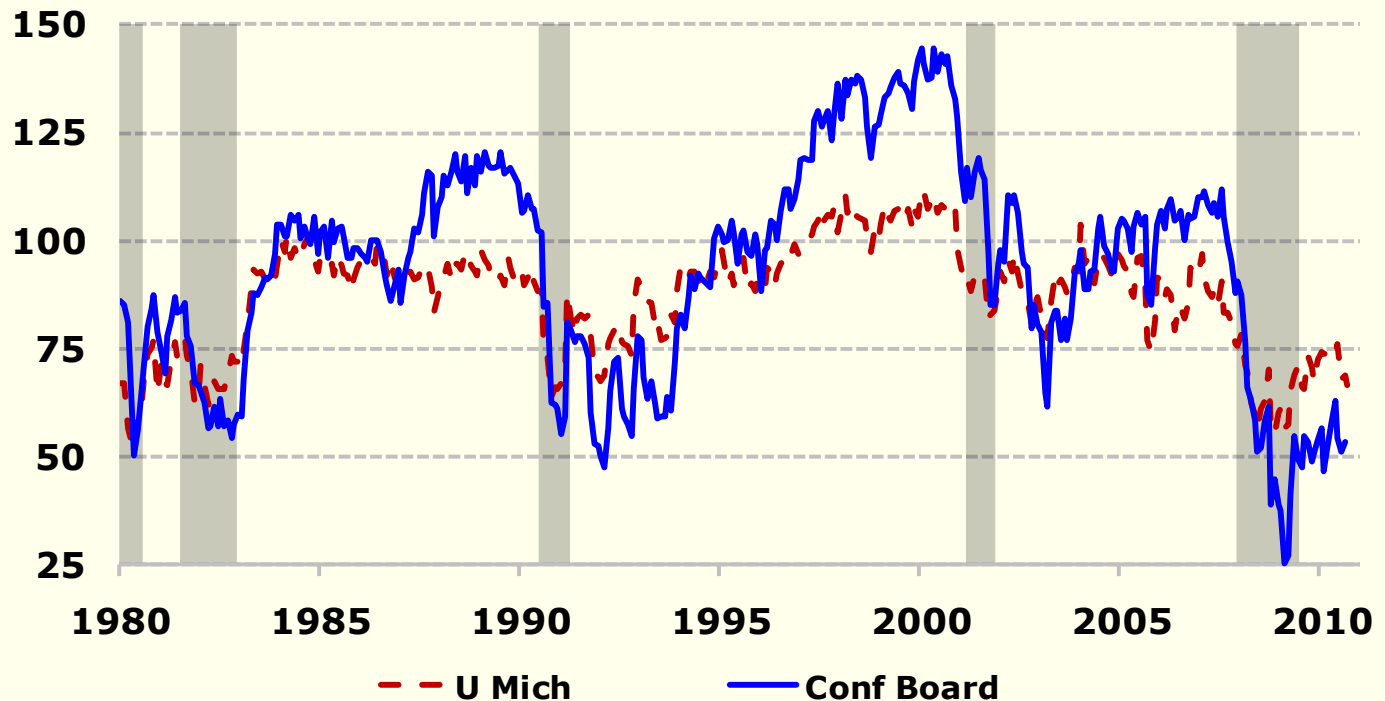


Consumer confidence remains uncertain

Index

Mich: 1966Q1 = 100, SA

Conf Board: 1985 = 100, SA

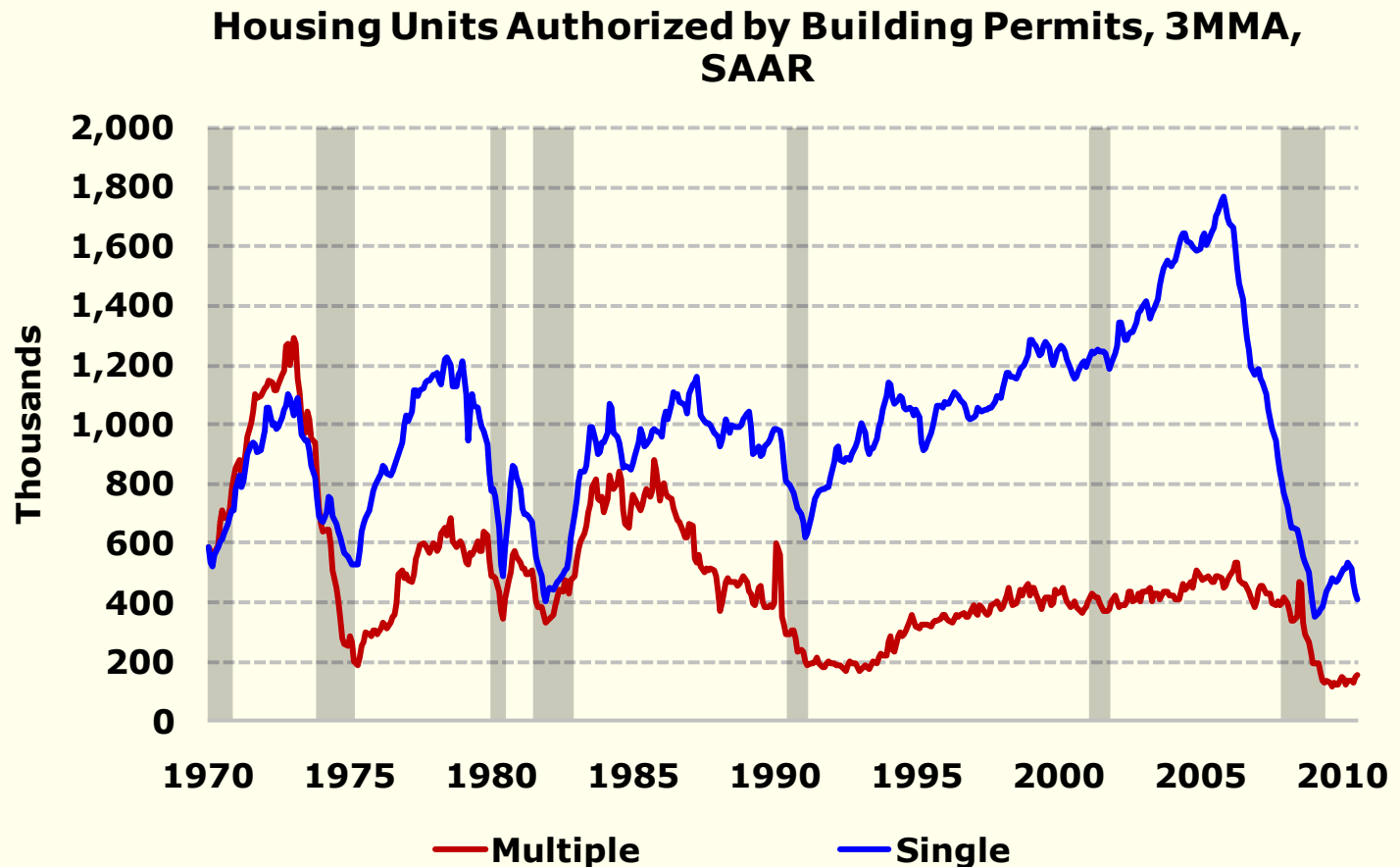


Source: University of Michigan; Conference Board, data through September 2010

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Building permits grew briefly from federal tax credits but remain low



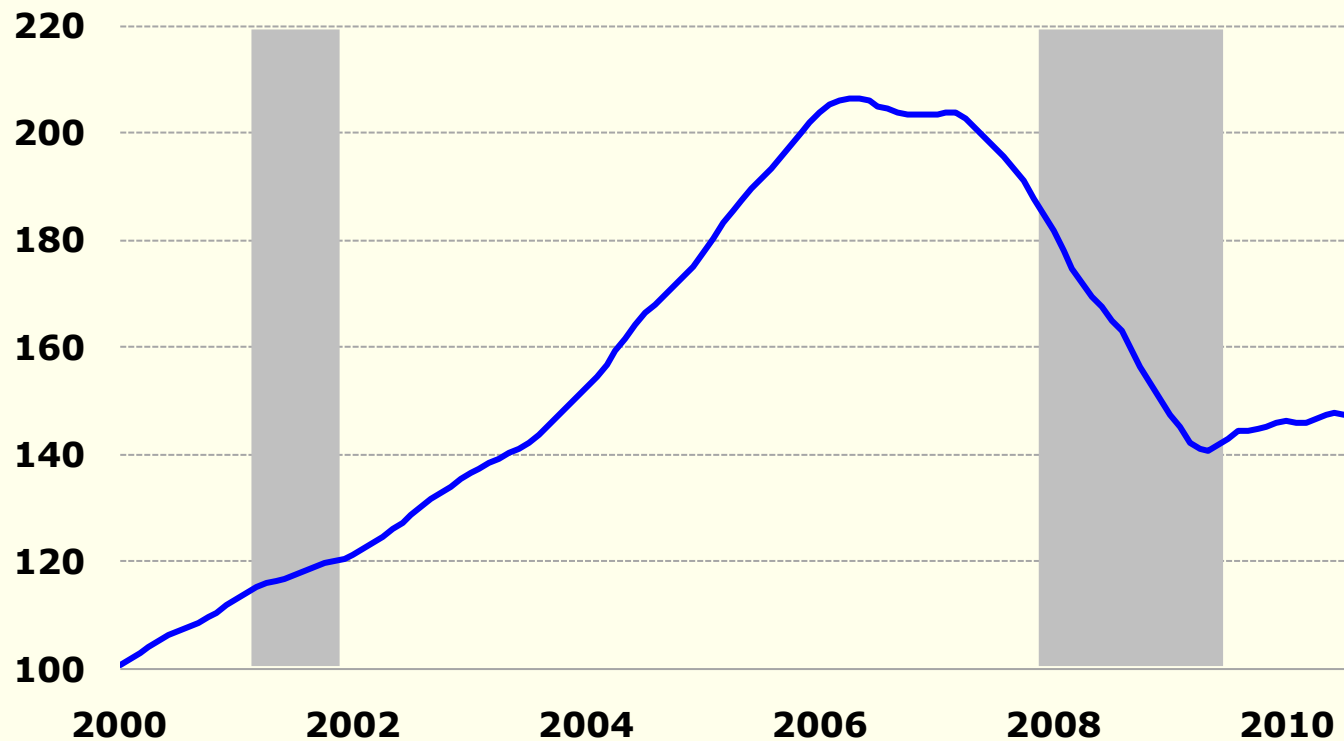
Source: US Census Bureau; data through August 2010

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Home prices are recovering but could slip again due to expiring tax credits

Case-Schiller 20-City Composite Home Price Index
(January 2000 = 100)

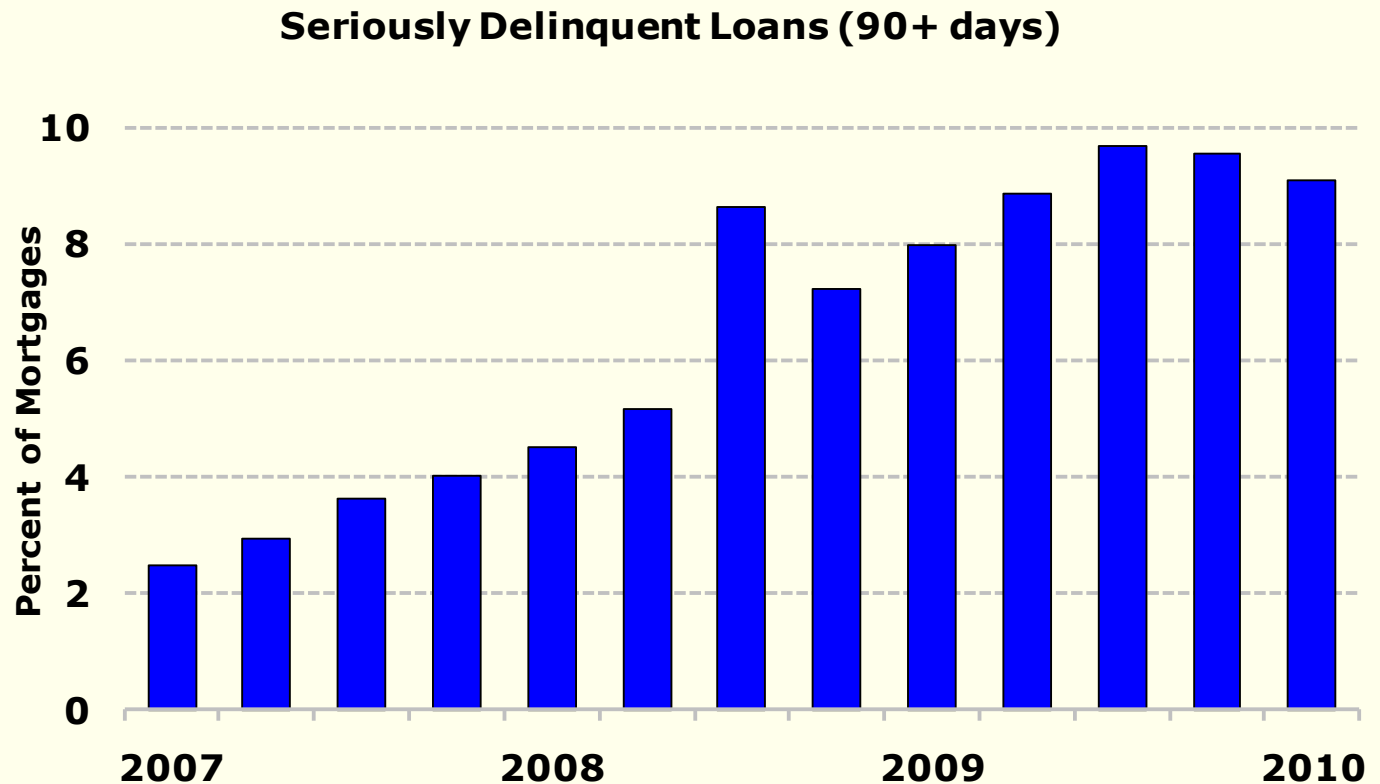


Source: Standard and Poor's; monthly data through July 2010

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The percentage of seriously delinquent mortgages is stabilizing



Source: Mortgage Bankers Association® National Delinquency Survey, data through 2010 Q2

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Foreclosure starts are decreasing



Source: Mortgage Bankers Association® National Delinquency Survey, data through 2010 Q2

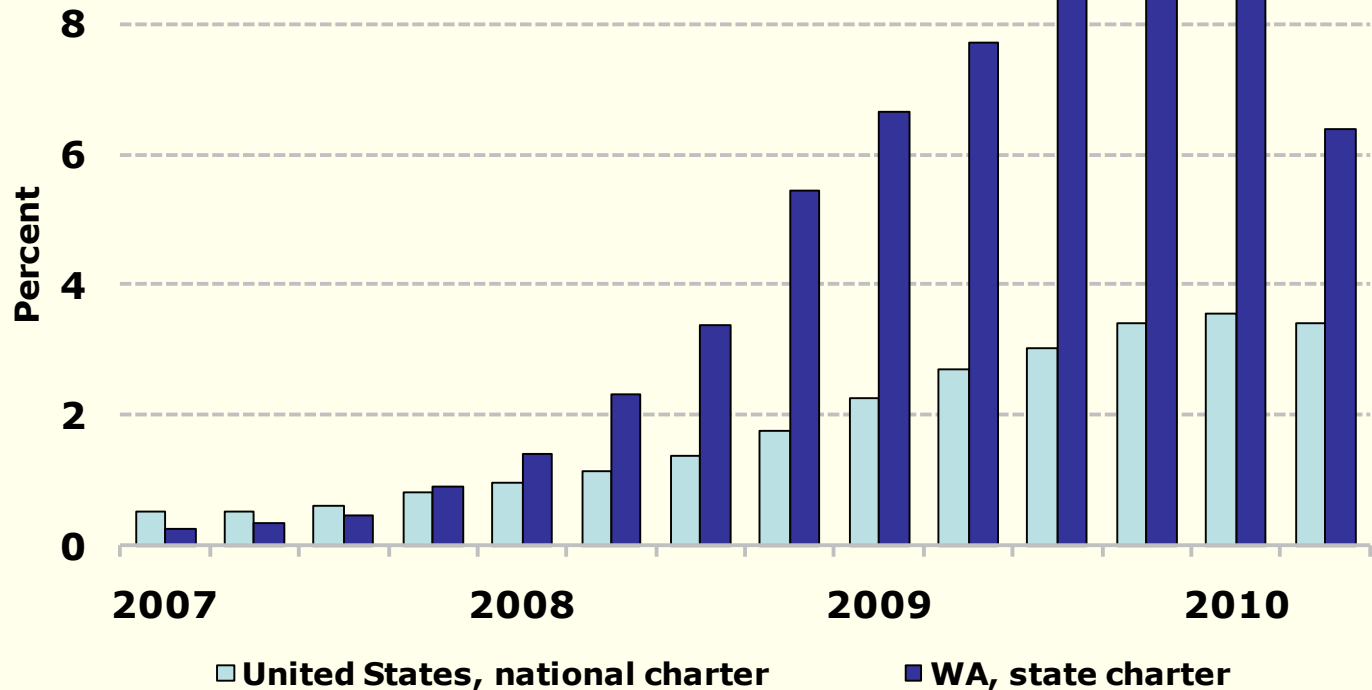
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Asset quality of banks is improving

The poorer asset quality of regional banks is due to their disproportionately high exposure to commercial real estate

Ratio of Non-Performing to Total Assets

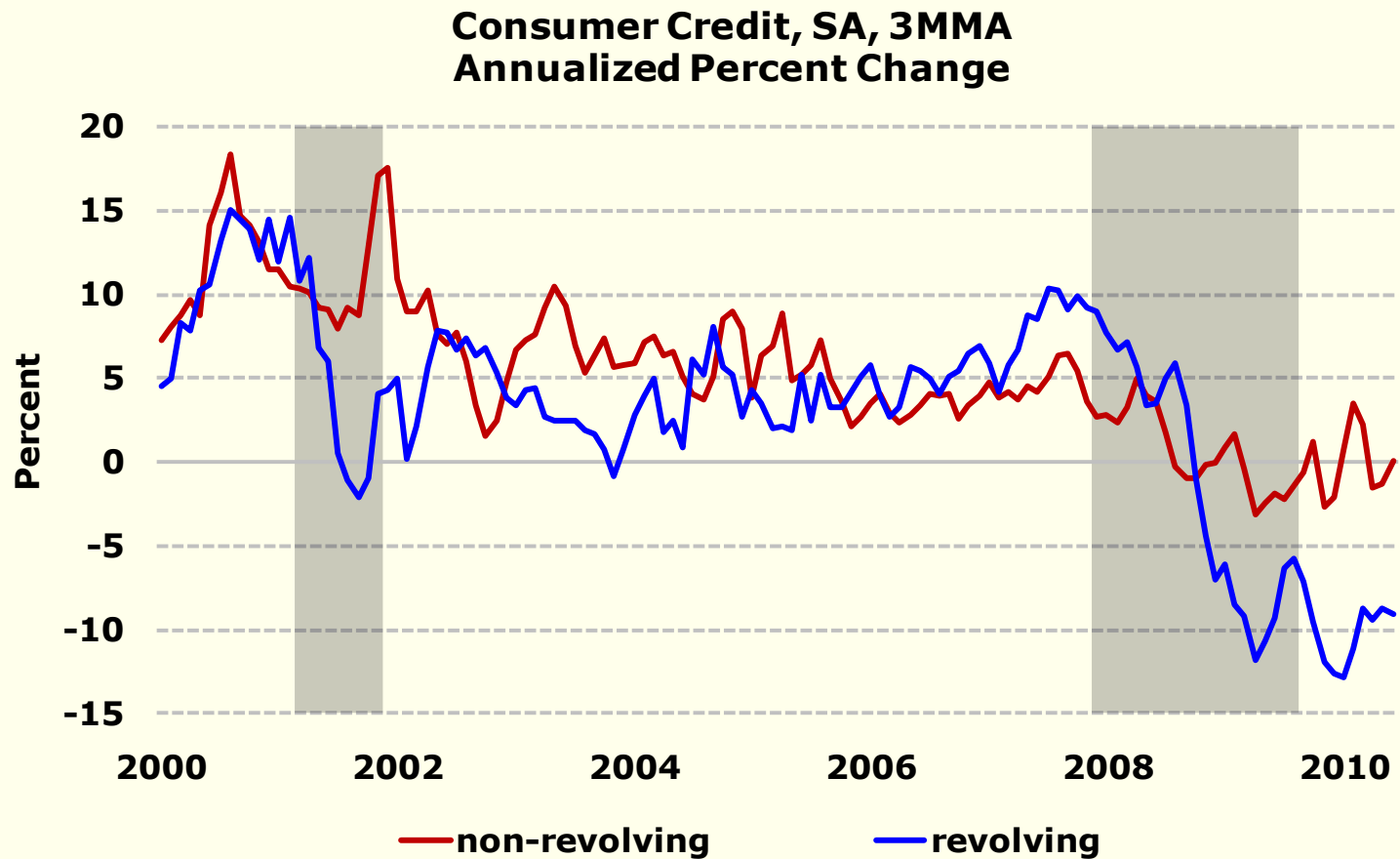


Source: FDIC, data through 2010 Q2

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Credit card debt is declining due to defaults, lower spending and payoffs



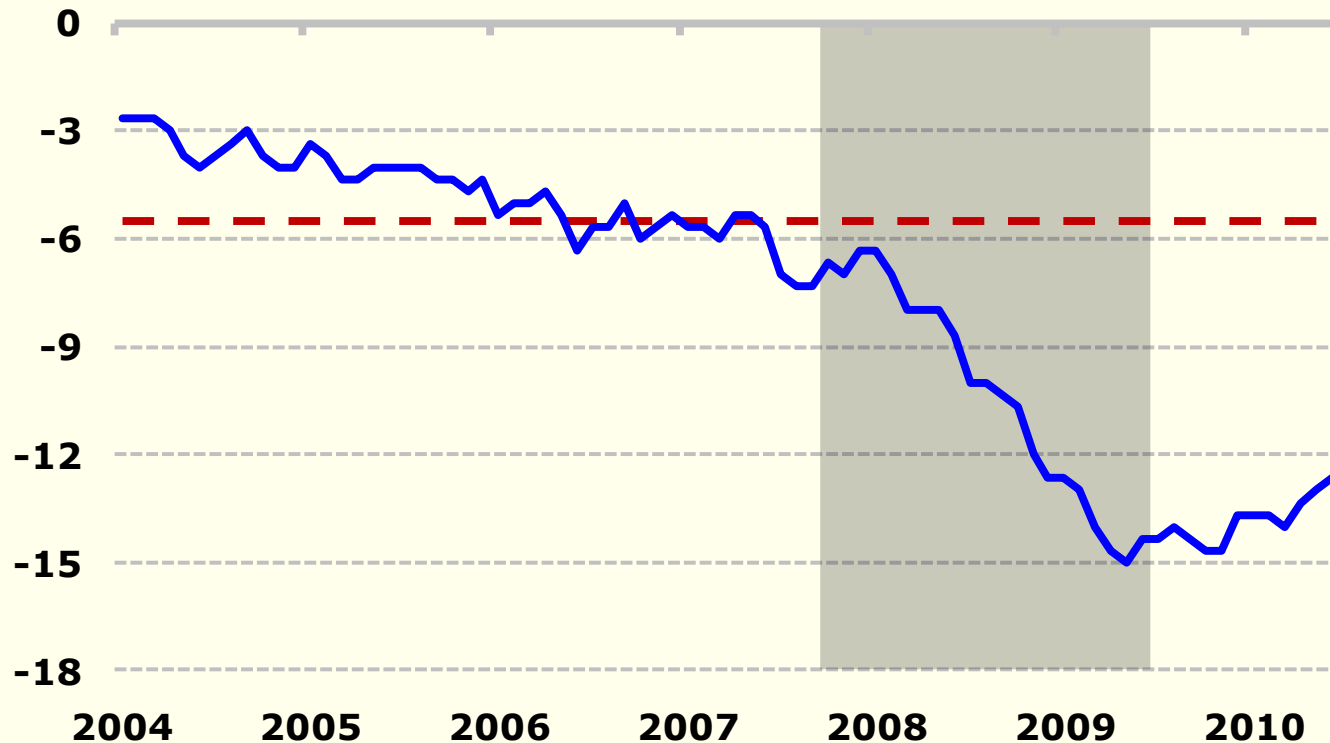
Source: Federal Reserve; data through June 2010

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Credit conditions for small business are improving, but remain tight

**Availability of Loans
Net Percent ("Easier" minus "Harder"), 3mma**



Source: National Federation of Independent Business; data through August 2010

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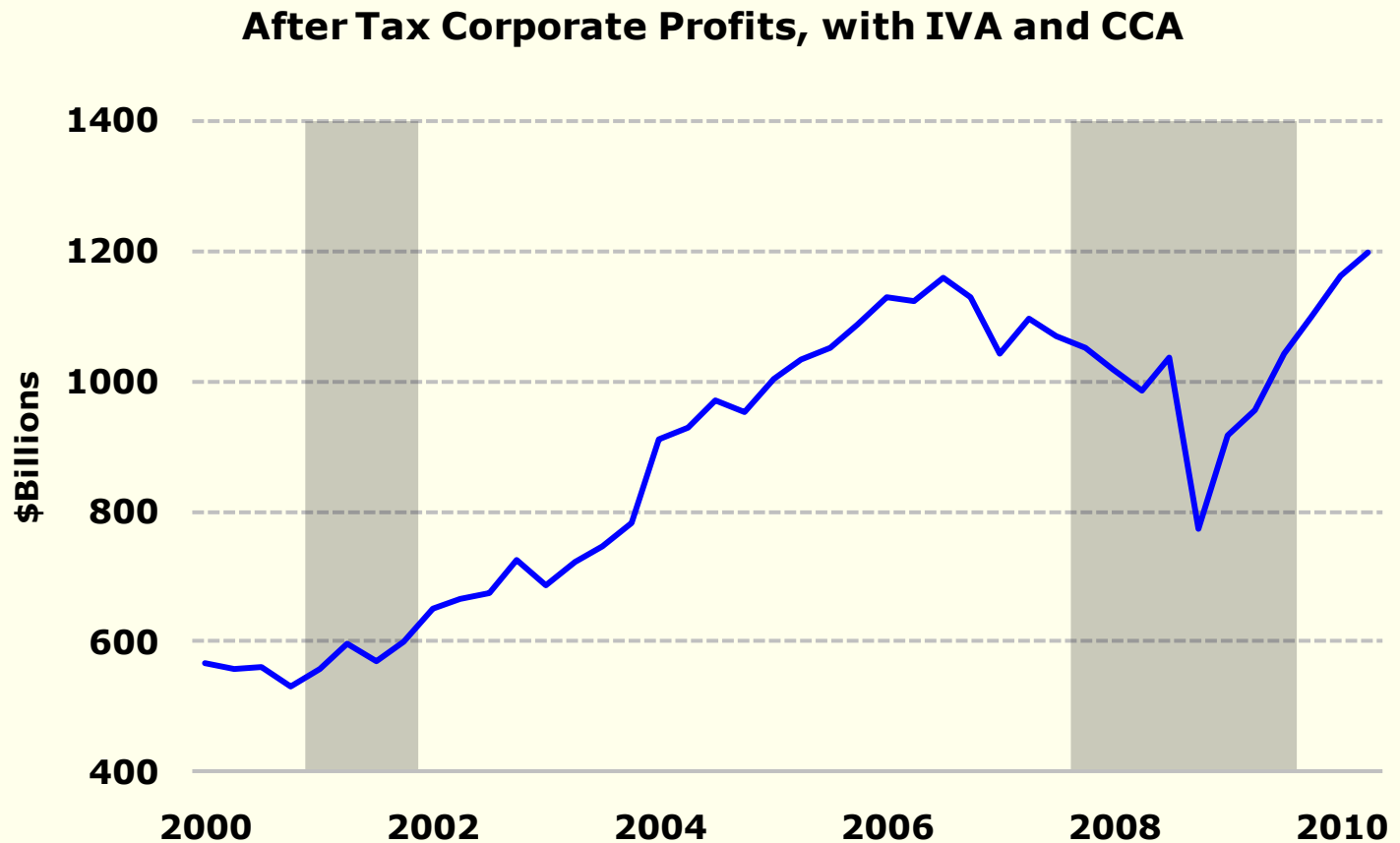


Corporate profits are back up above pre-recession levels

IVA:
Inventory
valuation
adjustment

CCA:
Capital
consumption
Adjustment

With IVA &
CCA, implies
profits from
current
production



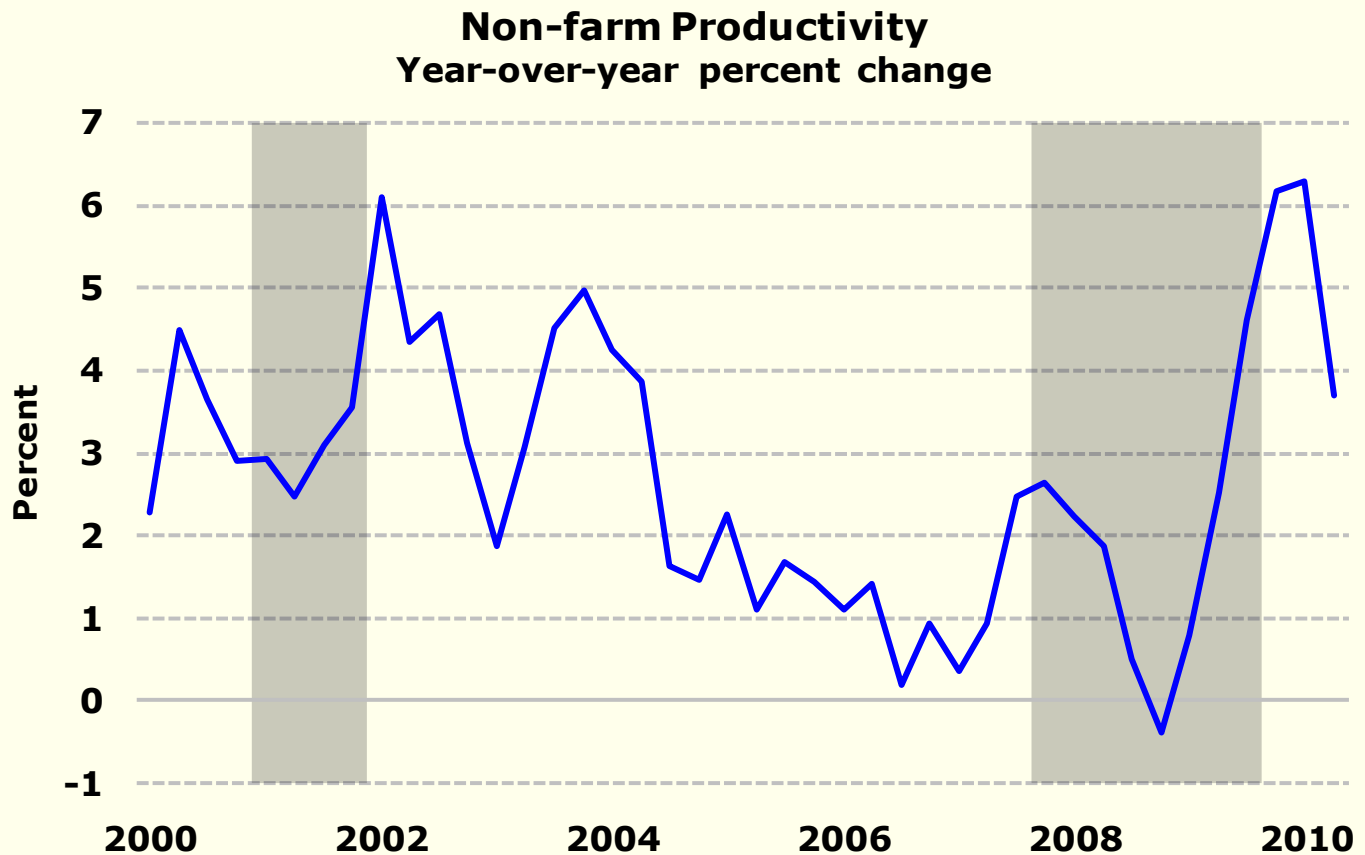
Source: BEA; data through 2010 Q2

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Productivity gains are slowing

This indicates the possibility of higher employment growth as demand strengthens

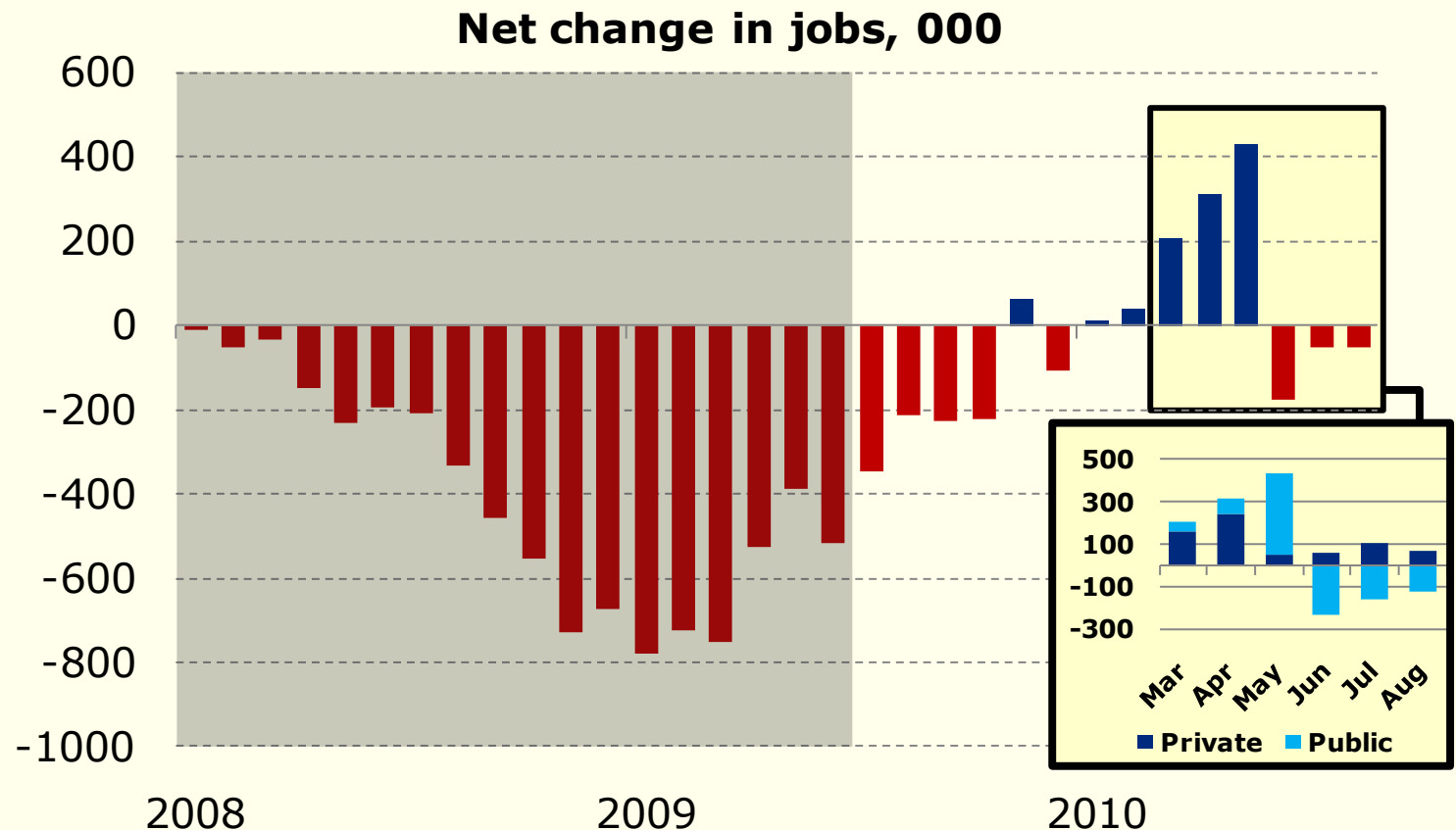


Source: US Bureau of Economic Analysis; data through 2010 Q2

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Temporary Census jobs obscured private job growth, which has slowed

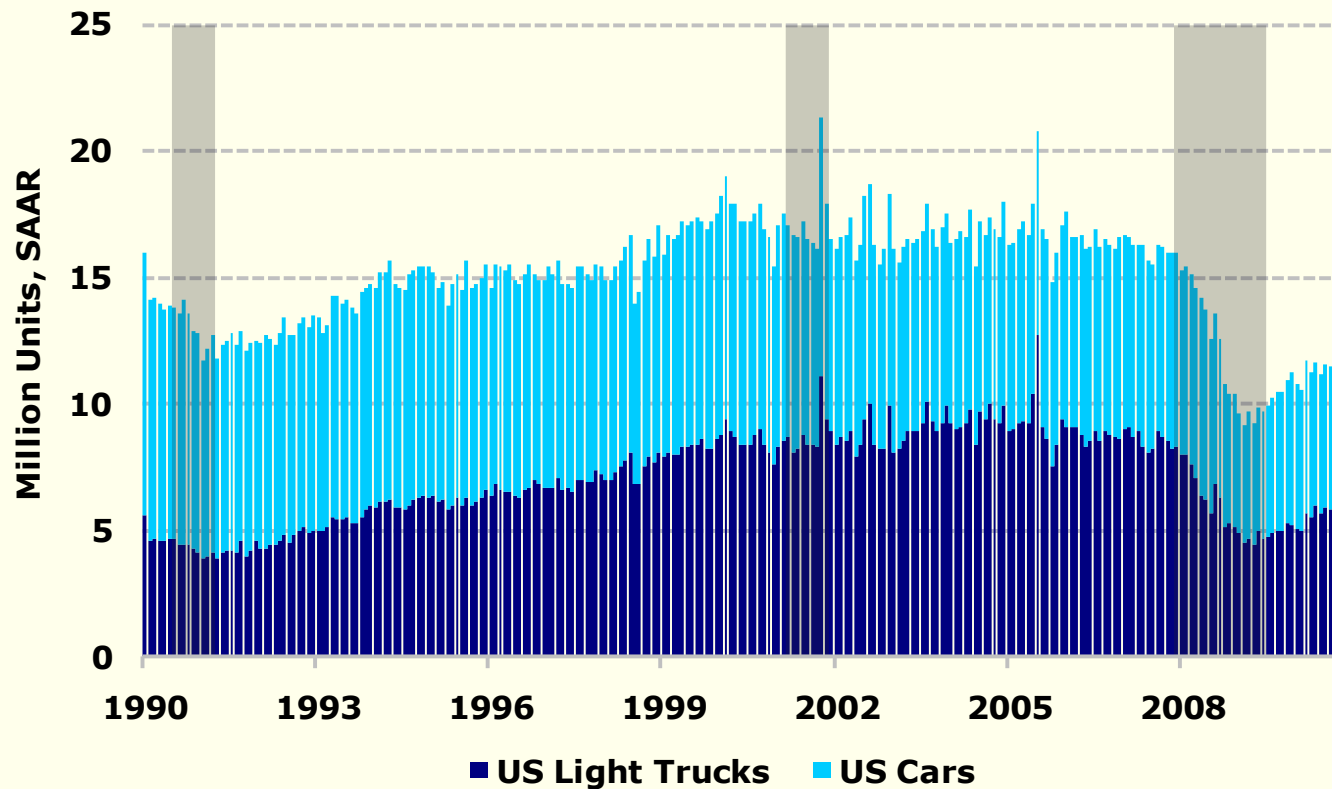


Source: US Bureau of Labor Statistics, data through August 2010



Automotive sales are treading water, after recovering from trough

**Cash for
Clunkers
effect
removed**



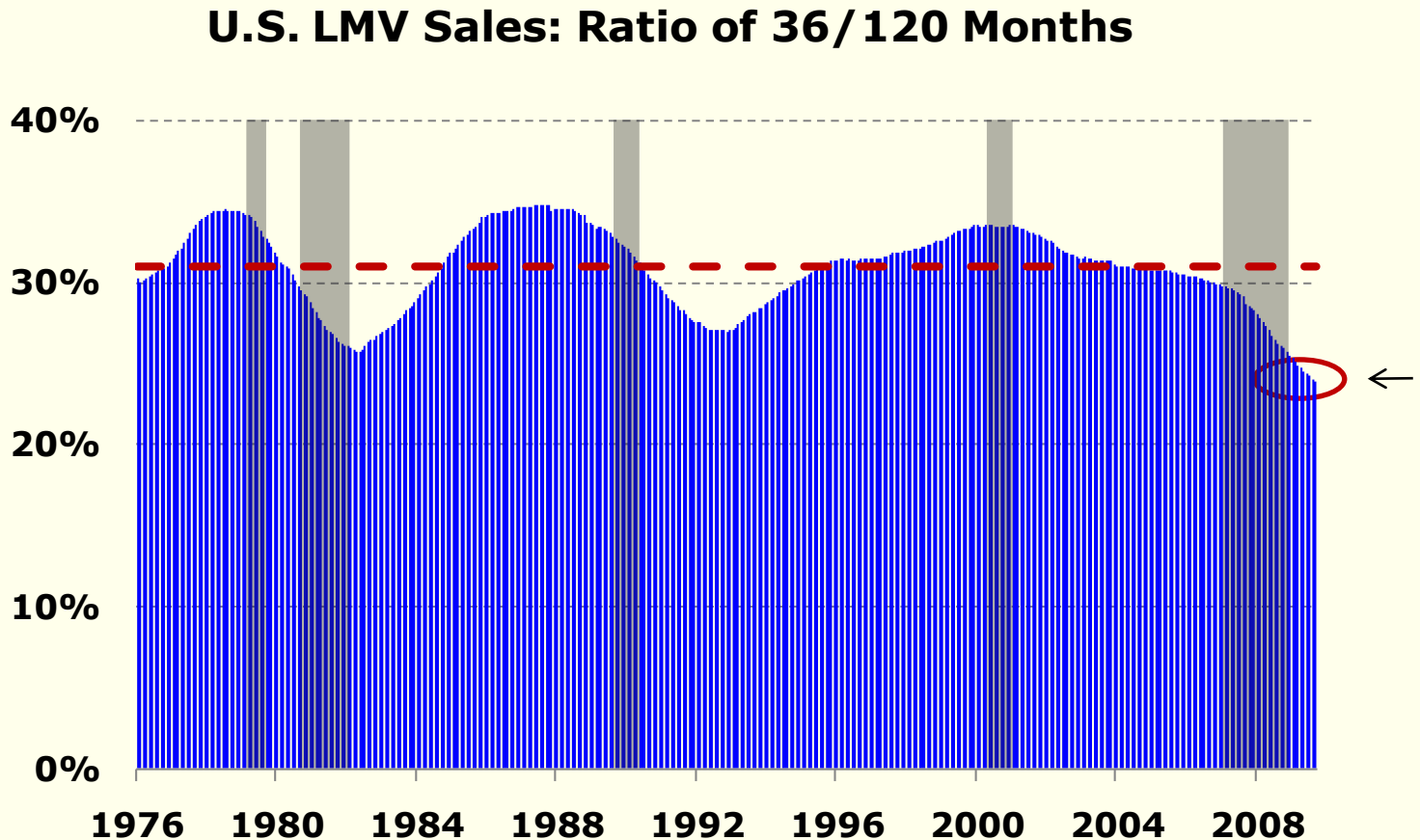
Source: Autodata Corporation; data through August 2010

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Relative age of the car fleet indicates continued turnaround in car sales

The percent of "old" cars on the road is at a historic high

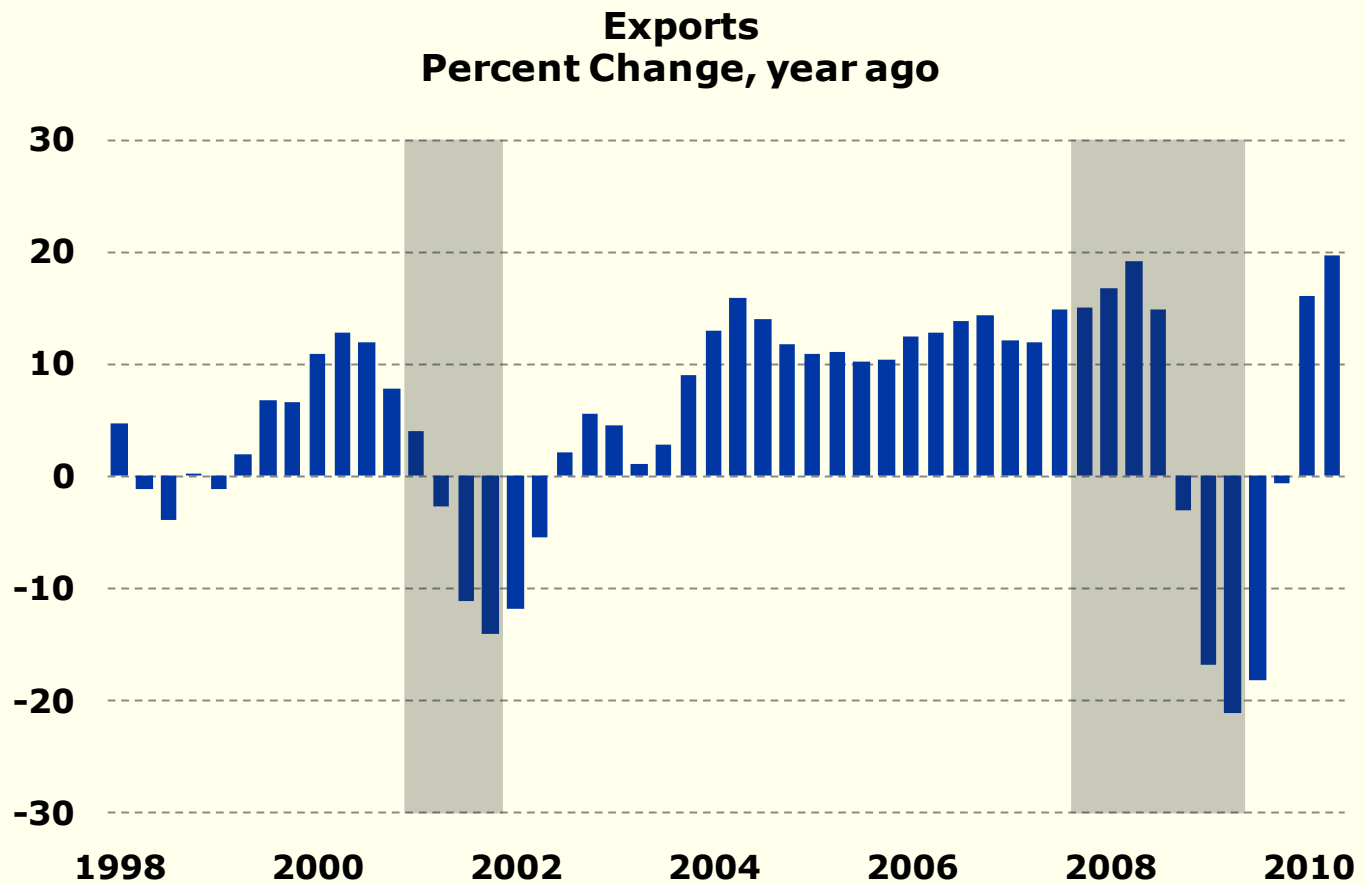


Source: Autodata Corporation, ERFC; data through July 2010

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Global economic recovery is boosting exports



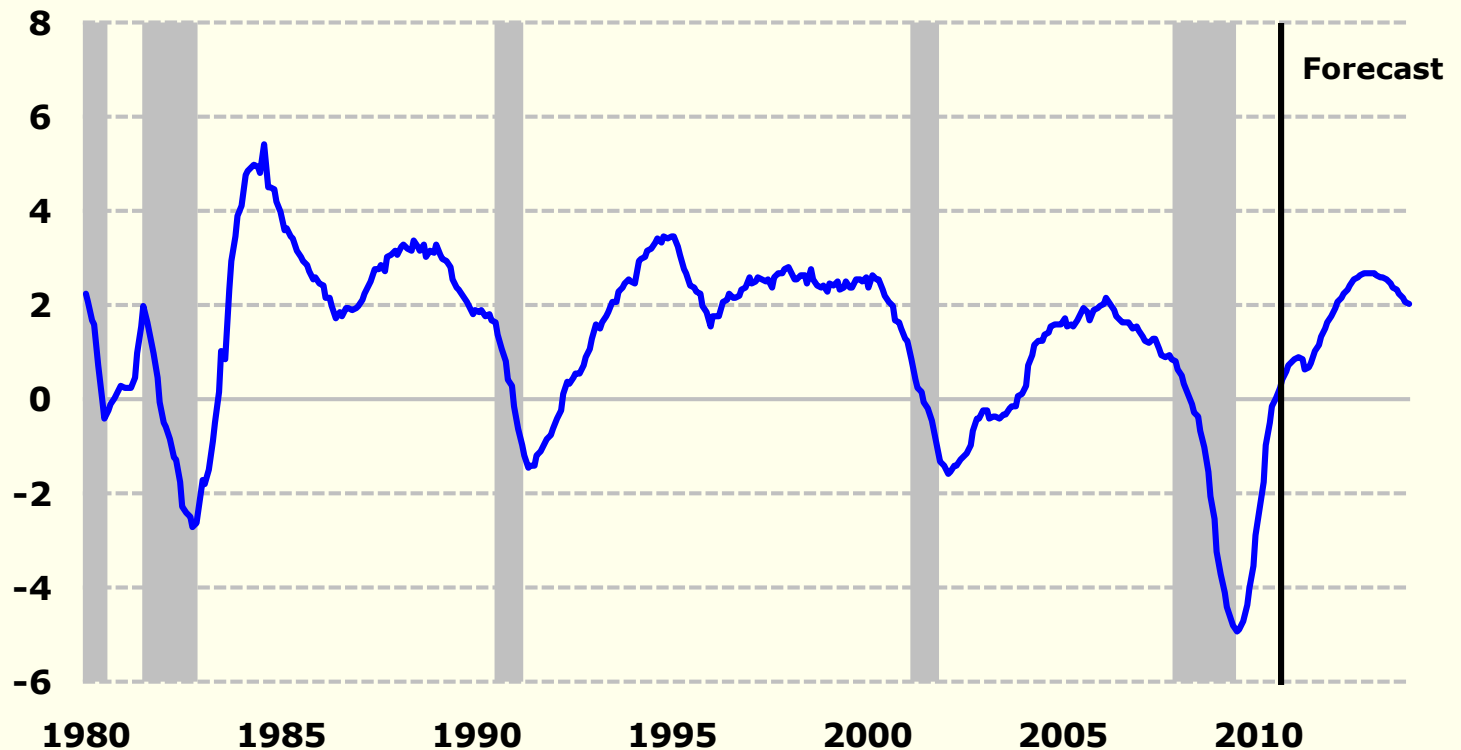
Source: US Census Bureau; through 2010 Q2

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US employment is forecasted to grow moderately through 2011

Percent change, year ago



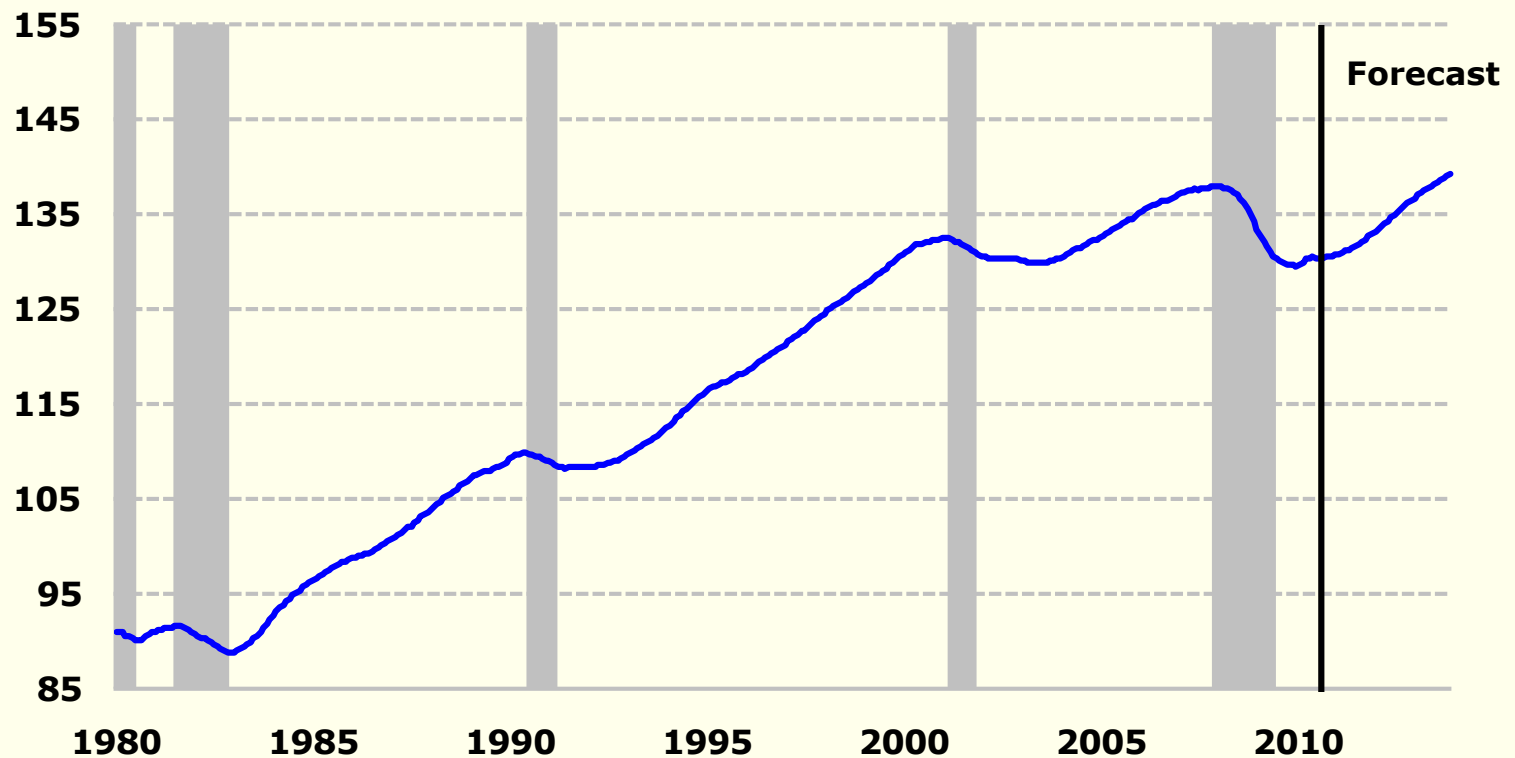
Source: ERFC September 2010 forecast; actual through August 2010

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Employment will not reach its pre-recession peak until mid-2013

Employment, millions



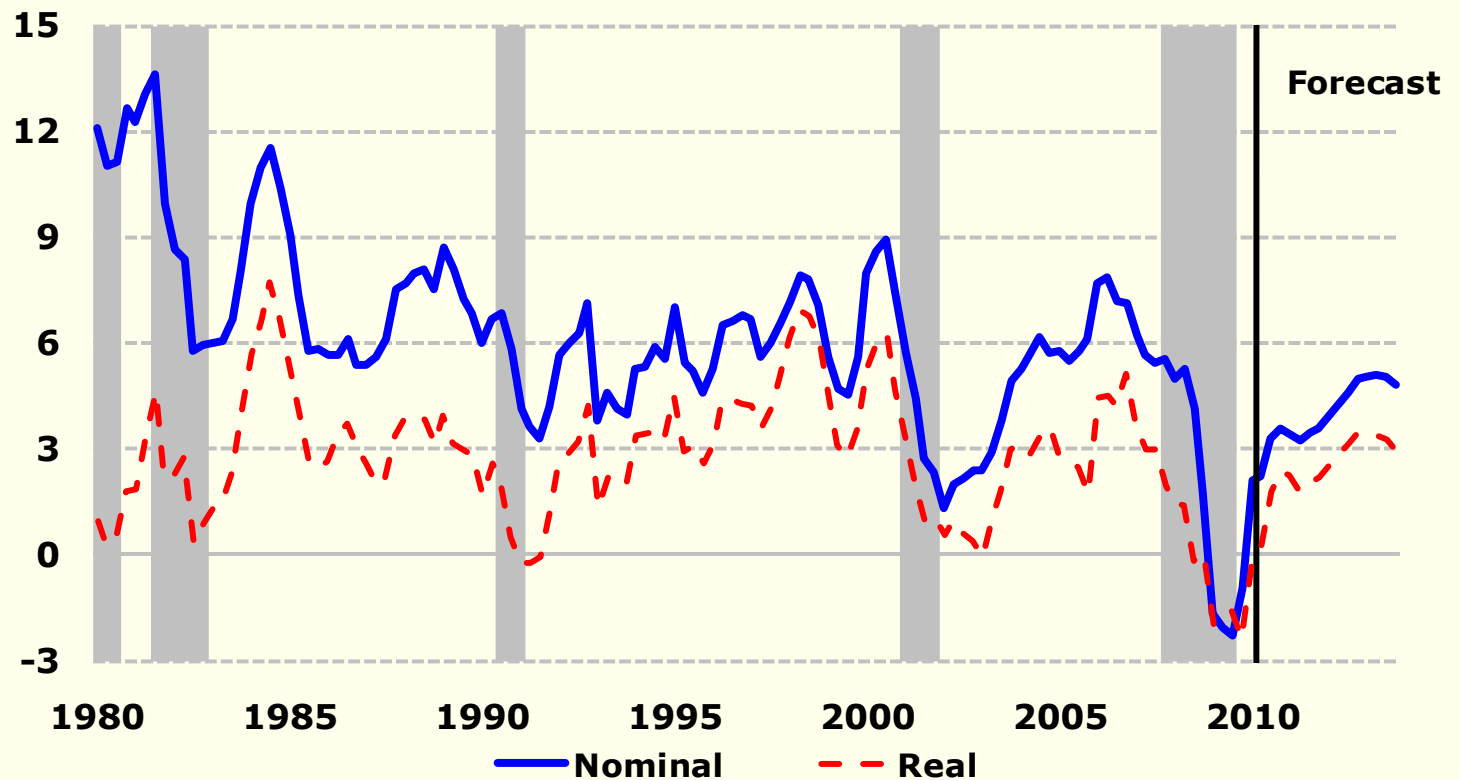
Source: ERFC September 2010 forecast; actual through August 2010

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Personal income growth is also expected to be modest through 2011

Percent change, year ago



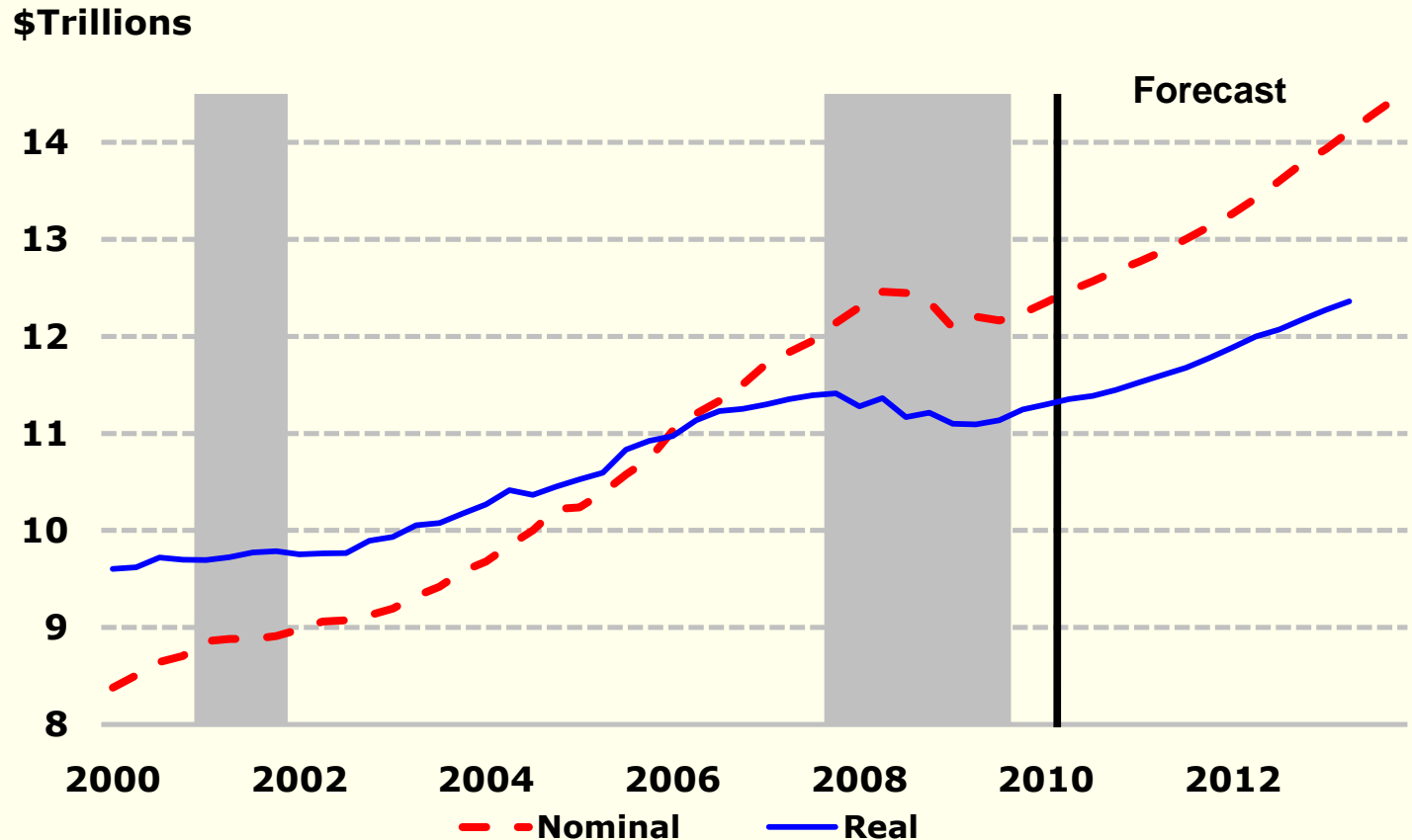
Source: ERFC September 2010 forecast; actual data through 2010Q2

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Real personal income won't exceed pre-recession peak until 2011Q2

Nominal personal income exceeded its pre-recession peak in 2010Q2



Source: ERFC September 2010 forecast; actual data through 2010Q2

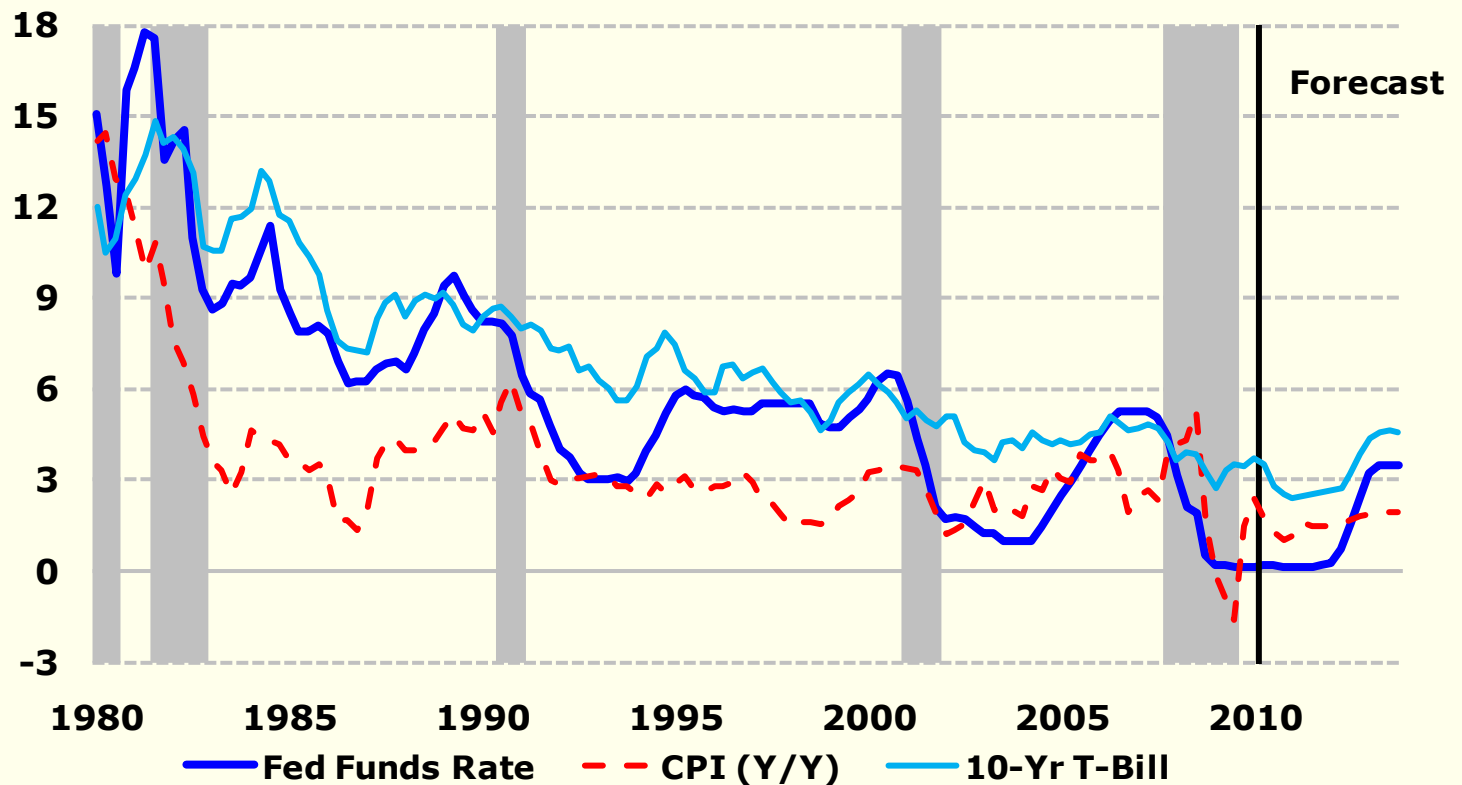
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Interest rates and inflation will remain low for some time

The Federal Reserve is not expected to raise interest rates until mid-2012

Percent change, year ago



Source: ERFC September 2010 forecast; actual data through 2010Q2

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Conclusion

- The economic recovery is going to be a slow painful slog, and it is difficult to see what is likely to cause growth to accelerate
- Inflation and interest rates will remain low for some time
- There is considerable downside risk and uncertainty in our forecast.



Questions



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